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SUBJECT: CRISIS ON LAYAWAY: THE POLITICAL IMPACT OF THE
STABILIZATION PACKAGE

REF: A) BUDAPEST 1059 AND PREVIOUS

Classified By: P/E COUNSELOR ERIC V. GAUDIOSI; REASONS 1.4 (B) AND (D)

11. (SBU) Although the Parliament continues to debate the implementing measures necessitated by Hungary's agreements with the IMF and EU (ref a), contacts are beginning to cautiously survey the longer-term landscape after weeks of crisis management.

CONTROLLING THE NARRATIVE

12. (SBU) For the Gyurcsany government, the latest characterization is one of a crisis that they solved but did not cause. Identifying Hungary's near meltdown as "two-thirds the result of foreign influences and one-third the result of domestic political opposition," the government is clearly seeking to portray itself as having delivered the international assistance required to stabilize the economy.

13. (C) The government has done little, however, to go beyond stabilization to structural reform. Defense Minister Szekeres dismisses the PM's actions to date as "theater - and bad theater at that," and Debrecen Mayor Lajos Kosa has archly dubbed Gyurcsany "Conference Planner-in-Chief" for the government's focus on discussion rather than action. Indeed, at a time when many are calling for broader government activism, Gyurcsany has publicly defined the government's role as limited to obtaining EU subsidies and building export markets while Hungary's Monetary Council promotes economic growth.

14. (SBU) Investors and economic analysts continue to decry the government's failure to pursue further reforms. Sandor Demjan, investment mogul and one of Hungary's richest citizens, notes that the stabilization package "is like an oxygen mask for a patient. It will not heal him, it is not an operation", and argues that "much deeper and fundamental changes are needed...reforms must be seen through even if they come with painful consequences." Among the reforms Demjan argues for is to revamp the social welfare system to ensure only those that truly need assistance are supported. Describing the current system Demjan noted that "the safety net below acrobats is there only for them," and not for "throwing anyone in from the audience."

15. (C) The government's approach, however, is paying early dividends with higher approval ratings for both the MSzP in general and the Prime Minister in particular. Polling commissioned by the Prime Ministry shows 63 percent of the public supporting the bailout. The Socialists have been further buoyed by our election results, which they regard as portending what they are careful to describe as an "even better relationship" with Washington.

16. (C) Still, the Socialists, while upbeat, are by no means united. MP Attila Mesterhazy notes that Gyurcsany still remains "the least bad option" for the party, and Defense

Minister Szekeres is once again hinting broadly that the PM can't win in 2010 - while he could.

A TWO-MINUTE DRILL?

¶7. (C) But 2010 may not be the operative date. Although he still regards "another two years of muddling through" by the Gyurcsany government as the most likely scenario, FIDESZ Parliamentary Faction Leader Tibor Navracsics believes that the Prime Minister could decide to call for early elections next summer if he wins reelection as MSzP Party President next March. One FIDESZ source confided that the party had even floated early elections as a condition of supporting the stabilization package; others have suggested that a new government should have been among the IMF's conditions. Many in the party, however, fear Gyurcsany's campaigning skills and are inclined to be careful of what they wish for.

JUST THE TWO OF US

¶8. (C) We note that both MSzP and FIDESZ sources are increasingly confident in writing off the smaller parties. Although the SzDSz and MDF still wield a degree of influence as the swing votes required to pass legislation in Parliament, polling continues to suggest that neither will survive the next election and members of both parties are admitting their concerns in private. Divided as always, Hungarians are deserting the smaller parties - and at the same time polls indicate they are concerned by the evolution of a two-party system.

PLACE YOUR BETS

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¶9. (C) While they may agree that they will be the only two parties left standing, the MSzP and FIDESZ are drawing very different conclusions from the past weeks.

¶10. (C) For the MSzP, their best chance is to emphasize their ability to deliver international assistance and to ensure that austerity measures are equitably imposed. Equitably, but perhaps not indefinitely: given the very strong popular opposition to spending reductions announced thus far - particularly among the pensioners who represent 20 percent of the electorate - we cannot help but suspect that the government will revisit its decisions before the next elections. As Krisztian Orban of the Oriens Consulting Group observes, "the Hungarian state has gone from parasite to predator," dependent on a "vicious circle" of taxing investors to finance its domestic spending. "Thank God for the Stabilization Package," Orban concludes, "but Heaven help us since the government will choose the votes of pensioners and the unemployed" over the advice of economists and investors.

¶11. (C) FIDESZ is apparently betting that its criticism of the stabilization package and support for tax cuts will play better with voters who dislike the spending reductions (and with investors who dismiss the government's commitment to reform). At a briefing for the Diplomatic Corps on November 13, FIDESZ officials warned of the risk of a "social crisis" if power remains in the hands of a government that "lacks credibility." Political Capital analyst Krisztian Szabados believes that FIDESZ is prepared to risk its "international political credibility" in the short term in order to pursue this approach.

CRISIS DEFERRED

¶12. (C) Comment: As Political Capital analyst Krisztian Szabados observes, the danger of explosion is over but the risk of longer-term implosion is not. But the economic crisis has given Hungary's parties something else to fight about rather than something to agree about. The government did move quickly to secure economic assistance, receiving

what one senior AmCham official called "a reward for years of bad economic policy." They will now try to do the same in search of political advantage. The combination of a stronger - but still weak - government eager to deflect blame and an opposition eager to criticize gives little hope for consensus. Without it, the stabilization plan will have deferred - but by no means solved - the pressing problems confronting Hungary. As Krisztian Orban concludes, "the bail-out has bought us one year ... but without reform we will remain one giant sub-prime mortgage." End Comment.
Foley